S.953 (Hoylman-Sigal)/A.1971 (Kelles)

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BILL	S.953 (Hoylman-Sigal)/A.1971 (Kelles)
SUBJECT	Business Tax Increases
DATE	February 24, 2025
OPPOSE	

The Business Council strongly opposes this legislation that would impose hundreds of millions in increased taxes on both corporations and small and mid-sized businesses doing business in New York State. The sponsors' justifications are based in part on claims of inadequate federal aid to states (even though federal funds to New York increased by 44% from pre-pandemic SFY 2022 compared to projected levels for SFY 2026), and inadequate state spending (which over the same period increased by 40%, nearly double the inflation rate.)

The bill's sponsors also make the curious argument that since (in their view) the federal corporate income tax rate is too low, New York State should punish businesses operating in New York State with significantly higher taxes – even though the state's corporate franchise tax receipts are at an all-time high, impacted by multiple factors including an already-existing tax rate increase on higher-earning businesses.

The provisions of this legislation, in effect, penalizes New York business taxpayers for taking advantage of federal tax provisions disapproved of by the bill's sponsors, including amendments that that specifically target small and mid-sized businesses for higher taxes – an approach being taken by few, if any, other states.

In fact, this bill sets apart New York's taxation of corporations and small and mid.-sized businesses in significant ways, including by reducing the benefit of measures designed to maintain a more competitive tax code that were adopted with broad, bipartisan support in the New York State legislature.

We believe it would be counter-productive to impose even greater tax burdens on private sector business, especially as we see other states adopting tax reductions.

For these reasons, and as detailed below, The Business Council strongly opposes S.953/A.1971.

GILTI Exemption – Section 1 of this bill would reduce the corporate franchise tax (Tax Law Article 9-A) exemption for "global intangible low taxed income" (GILTI) from 95 percent to 50 percent. The 95 percent deduction was adopted at the end of the state's 2019 state legislative session, and was the result of a bipartisan agreement to decouple from this provision of the federal "Tax Cuts and Jobs Act of 2017," or TCJA. (see Chapter 39, Laws of 2019, Part I). It also assured the equal treatment of domestic dividends and deemed foreign dividends under New York's Tax Law, avoiding an issue of likely litigation.

By backtracking on this provision, New York's treatment of foreign earnings would be inconsistent with the majority of states that employ broad conformity with the Internal Revenue Code as the starting point for calculating state-level tax liability. Virtually all "conformity" states have adopted a GILTI exemption of 95 percent or greater, including but not limited to Pennsylvania, Massachusetts, Connecticut and Illinois. All told, 28 states with a corporate income tax provide a GILTI exemption of at least 95%, including both "red" and "blue" states. (Note that this is not an issue in California, which is not a general a IRC conformity state, nor Texas, which conforms to the pre-TCJA version of the Internal Revenue Code for purposes of its franchise tax.)

The Business Council strongly supported New York's decoupling from the federal GILTI regime and strongly opposes this proposed legislation that would increase New York State taxation of foreign earnings that have yet to be paid to a New York corporate taxpayer. It would place New York Businesses at a competitive disadvantage not only domestically but globally as well.

The TCJA subjected a portion of undistributed earnings of foreign subsidiaries ("controlled foreign corporations," or CFCs) to ongoing federal taxation, as part of a multi-part tax reform package that included significant rate reductions and other beneficial measures. This provision (IRC §951A) established the concept of GILTI and was intended to impose federal tax on income earned in low-tax foreign jurisdictions from "intangible" property, such as patents, copyrights, and trademarks. However, GILTI is actually a tax on the overall business income of foreign subsidiaries that is not actually distributed to the U.S. parent, as it is calculated as a function of the taxpayer's foreign fixed assets, and not actual earnings from intangible assets in "tax havens." Moreover, at the federal level, the impact of GILTI is partially offset by federal tax credits that would not be replicated at the state level under this legislation.

New York State's corporate franchise tax has long exempted this type of undistributed income of domestic and foreign subsidiaries. However, due to the way the federal law was drafted, GILTI was not covered by New York's then-existing statutory exemption. Therefore, New York's tax law – left unamended –

would have required GILTI to be included in the tax returns of New York business taxpayers and would have resulted in discrimination of foreign versus domestic income.

Without an exemption, New York corporate taxpayers would be subject to state-level tax on income that has not, and may never actually be, received by the New York taxpayer. In addition, the State tax levy is not reduced by the foreign tax credits allowed at the federal level, nor by the federal rate reductions – provisions of the federal TCJA that offset the GILTI tax, that were not replicated at the state level.

There are compelling reasons why New York should maintain its 95 percent GILTI exemption from state-level taxation under its corporate franchise and insurance taxes. This approach is consistent with New York's policy of not taxing the earnings of foreign subsidiaries when those earnings have not been distributed to a New York taxpayer. Imposing State taxes on foreign earnings will adversely impact New York's business climate. It will be contrary to the State's efforts to retain and attract multi-national businesses and will set New York apart from the majority of states which exempt GILTI from state-level taxation.

Corporate Franchise Tax Rates – Section 2 of this legislation would increase the marginal corporate franchise tax rate on net income to 8 percent for taxpayers with a business income base of over $2.5 million, to 12 percent of a taxpayer's business income base in excess of $10 million, and to 14 percent of a taxpayer's business income base in excess of $20 million. At present, the general Article 9-A rate is 6.5 percent, however a temporary rate of 7.25 percent applies to corporations with taxable income over $5 million for the 2021 through 2026 tax years.

This proposal would vault New York to the top of the list of corporate tax rates among the states, higher than New Jersey which presently has the only rate above 10 percent.

For corporations operating in New York City, these increased state tax rates would also be on top of the City's corporate tax of 8.85 percent (on income apportioned to the city), or 9 percent for financial corporations, increasing the top marginal rate in New York to over 20 percent.

These rate increases only apply to C-corporations, whose earnings are also subject to progressive income tax rates once paid to shareholders. Dividend payments to shareholders are not deductible business expenses for the corporation, but once received by shareholders those dividend payments are subject to progressive taxation at the federal, New York State and – if applicable – New York City level under those jurisdictions' personal income tax laws. The result is that C-corporation profits are subject to two levels of taxation, including under already progressive personal income tax laws, and this bill would exacerbate that double-taxation effect.

There is no compelling tax policy reason to impose progressive corporate franchise tax rates, as a corporation's level of taxable income does not reflect their relative profitability, i.e., profits as a percentage of total sales, nor does their taxable income reflect the ability to pay of their shareholders (which includes many whose shares are owned in public or private retirement funds.)

New York's permanent corporate franchise tax rate of 6.5 percent is somewhat competitive, being "only" the 21st highest among the states. However, it still adds to a very high total business tax burden in New York. A recent study by the Council on State Taxation (an association of business tax professionals that advocates on state tax structures but not tax rates) showed that combined state and local taxes paid by New York businesses totaled $90.3 billion, nearly as high as Texas (at $90.9 billion) - a state with a significantly larger state economy and workforce - and almost double Florida's combined business tax burden. On a per-employee basis, New York's combined tax burden on business was $12,100 per employee, second to only North Dakota (whose tax revenues are skewed by high extractive industry taxes), and 55 percent above the national average.

Importantly, other states are taking a different approach. In contrast to New York's proposal, a number of states are reducing their business taxes. Among other northeast states, For example, Pennsylvania reduced its corporate tax rate from 9.99 percent to 8.99 percent effective January 1, 2023, and will continue to reduce the rate by 0.5 percentage points each year until it reaches 4.99 percent at the beginning of 2031.

From an economic policy perspective, we believe it is the wrong time to impose additional costs on employers. From a tax policy perspective, we believe this proposal make little sense.

Pass Through Entity Tax – Part 4 of this legislation would significantly reduce the effectiveness of New York's mechanism to restore federal deductibility of state taxes on the income of non-incorporated businesses. Specifically, it would reduce the value of the personal income tax credit for pass-through entity tax from 100 percent to 75 percent of the pass-through entity tax.

The "pass through entity tax" (PTET) and the related tax credit was adopted in 2021 (see Chapter 59, Laws of 2021, Part C) to benefit New York's mostly small and mid-sized unincorporated businesses, which were adversely impacted by the cap on state and local tax deductions included in the TCJA.

Generally speaking, unincorporated businesses are not subject to income tax at the entity level. Instead, their income is attributed to the business owners (whether or not the income is actually distributed to such owners) and taxed under the state's progressive personal income tax.

In the wake of the TCJA, states took steps to restore federal deductibility of state-imposed taxes. New York joined more than 20 other states (including California, Connecticut, New Jersey, Massachusetts, Illinois, Ohio, Michigan, among others) to adopt a PTET. Under a PTET, an unincorporated business is subject to an entity-level income tax, with the impact of the tax "distributed" proportionately to its owners. Those owners are able to deduct their share of the PTET on their federal returns, while receiving a state tax credit equal to their share of the state PTET payment.

The result is that New York State has no change in net revenues, as PTET income is offset by the PTET credit, and our state's small business taxpayers are restored to their pre-TCJA tax treatment.

Under this proposed legislation, the offsetting credit would be reduced to 75 percent of the PTET tax liability, which will ultimately result in a great State tax liability imposed on the owners of small and mid-sized businesses than the liability imposed prior to the enactment of the PTET statute

The PTET statute was designed to support New York State's small and mid-sized business community at no cost to the State by restoring deductibility of state taxes limited under federal tax reform.   This regime was adopted with significant bipartisan support in the New York State legislature. We see no compelling reason to effectively reducing this valuable tax benefit for small and mid-sized businesses.

Section 199A Tax - Section 5 of the bill would amend the state's personal income tax law by imposing an additional tax corresponding to the value of a taxpayer's federal deduction under IRC §199A. The rate would be set at the highest applicable federal personal income tax rate applicable to such income.

Section 199A is another provision of the Internal Revenue Code added by the TCJA. It provides a 20 percent federal income tax deduction for "qualified business income." This deduction is limited to joint return filers with under $315,000 in taxable income or single filers with up to $157,500 in taxable income (the deduction is phased out for joint return taxable income between $315,000 and $415,000 and for single filers with taxable income between

$157,500 and $207,500.) It only applies to income from domestic businesses, and those organized as a sole proprietorship, partnership, S corporation, trust or estate to qualify.

Importantly, New York State is decoupled from this provision of the IRC, meaning that small businesses do not receive a comparable deduction on their state-level personal income taxes.

Ironically, however, in approving the FY 2023 budget, the state legislature did adopt an increase in both the state and New York City personal income tax small business income exclusion from 5 to 15 percent of net business or farm income, and expanded eligibility to include LLCs, partnerships and sub-S corporations with total income up to $1.5 million.

In short, this provision of S.953/A.1971 imposes a state tax penalty on New York State small businesses for provisions of federal tax law that provides no state-level tax benefit, and more than offsets state-level small business relief approved just two years ago. We oppose this imposition of increased tax liability on small business and farm businesses.